



# WRNewswire

An AALU Washington Report

Tuesday, 29 July 2014

WRN# 14.07.29

The *WRNewswire* is created exclusively for AALU Members by insurance experts led by Steve Leimberg, Lawrence Brody and Linas Sudzius. The *WRNewswire* provides timely reports and commentary on tax and legal developments important to AALU members, clients and advisors, delivered to your inbox as they happen.

---

## **TOPIC: Policy Rescinded Due to Concealment of Drug Use**

**CITE:** [\*PWPG, LLC v Primerica Life Insurance Company\*](#), D065467, 2014 WL 3661110 (Ct. App. 4<sup>th</sup> Dist Div 1 CA, July 24, 2014).

**SUMMARY:** PWPG, LLC purchased a policy on the life of Herschel White, one of its principals. Although in the policy application, White denied having ever used or been treated for using illegal drugs, Primerica discovered—within the contestable period—a history of cocaine use. It rescinded the policy.

PWPG sued Primerica. It alleged breach of contract and bad faith.

But the lower court granted summary judgment in favor of Primerica because:

- (1) Primerica's policy application inquired about White's history of illegal drug use and counseling and/or treatment for that use,
- (2) White had a history of cocaine abuse and drug/alcohol counseling during the two years preceding his completion of the application,
- (3) White misrepresented and concealed his cocaine use and counseling on his application, and
- (4) White's history of cocaine abuse and counseling was material to the issuance of the Primerica policy.

The Court of Appeals agreed completely with the lower court and allowed the insurer's rescission of the policy.

**FACTS:** White, a chiropractor, was also a principal of PWPG, which owned property next to his chiropractic practice. On March 16, 2007, White met with a Primerica insurance agent and completed an application for a \$2 million life insurance policy.

A question in the application specifically asked:

In the past 10 years, has any person named in this application ...received professional counseling or medical treatment due to the use of; alcohol or drugs; used illegal or illegally obtained drugs; been convicted of drug or alcohol related charges; been convicted of a felony; or been incarcerated for any felony?

White answered “No.” He then signed the application, verifying that all information provided was true and complete and agreed that Primerica could void and rescind the policy within two years after its date of issuance if any information was determined to be false or incomplete. The application was also signed by PWPG as the policy’s owner.

As part of its underwriting process, Primerica had an independent company interview White by telephone to confirm his answers to the questions on the policy application. White was again asked,

In the past 10 years have you received professional counseling or medical treatment due to the use of alcohol or drugs?

Have you used illegal drugs or illegally obtained drugs?

To both questions, White responded: “No.”

Primerica issued the policy with a September 20, 2007 “date of issue.” The policy contained an incontestability clause which permits Primerica to contest the policy’s validity by rescission for material misrepresentation or concealment within two years after its date of issue.

PWPG learned in November, 2008 that White was dying from lung cancer. It submitted a claim under the policy’s “Terminal Illness Accelerated Benefit” rider for an advance payment of benefits.

Since the policy was within two years of its issuance, and thus within the two-year contestability period, Primerica conducted a routine investigation of White’s medical history. Primerica again requested all medical records pertaining to White from his health insurer, Kaiser. When Kaiser received that request, it produced a behavioral health record dated June 30, 2005, which had not been produced in response to Primerica’s initial records request to Kaiser during the original underwriting process. This record showed that on June 30, 2005, White underwent an assessment and was diagnosed with: “Cocaine Abuse ... R/O Alcohol Abuse ... Partner Relational Problem.”

At that point, Primerica attempted to contact White, directly and through a third-party vendor, Broyles Claims Decision Support, Inc. Broyles placed several phone calls to White at his office, but was unable to reach him. Broyles also sent a letter dated November 24, 2008, to White's residence via Federal Express, requesting that White contact Broyles for a recorded statement. White signed for the letter but never responded.

Primerica then determined that it would not have issued the policy had it known about White's history of cocaine abuse. Primerica sent letters on March 20, 2009 to White and PWPG, notifying them that it had rescinded the policy based on White's history of cocaine use and professional counseling for that use. The letter asked him to contact Primerica if he had any additional information he would like Primerica to consider. Neither White nor PWPG responded to that letter, either to challenge the rescission or to provide any additional information regarding the basis of the rescission; nor did White ever suggest that he was at all confused by the question in the application.

Primerica served subpoenas on Kaiser. In response it received more records further confirming that White had used cocaine extensively and received counseling from that institution as recently as June 2005. The records stated that White argued with his girlfriend over his "using cocaine," that he liked to use cocaine, that he had been using cocaine for at least two years, and that he feared he would lose his girlfriend over his habits. In one report, White stated he snorted "several lines" of cocaine once or twice per week, that he had been using cocaine for 11 years, his most recent use being the previous Friday, and that he had "cravings" for alcohol and cocaine. He was diagnosed with cocaine and alcohol abuse and referred for further treatment.

Primerica's written underwriting guidelines and underwriting practices provide that cocaine use by an applicant within two years prior to the application, regardless of amount or frequency, would result in the declination of coverage. Therefore, had Primerica known about White's cocaine use, it would not have issued the policy. Moreover, under Primerica's written guidelines, even if White's cocaine use were more remote (between two and five years prior to the date of the application) Primerica would not have issued the policy at the same premium rate. Primerica would have charged a significantly higher premium rate for the policy, amounting to an additional \$10,000 in premiums per year.

The lower court found that Primerica properly rescinded the subject Primerica life insurance policy based upon White's material misrepresentation and concealment on the insurance application.

The court here did not buy—and likely other courts in the future would not accept the argument—that the drug question on the application was ambiguous and could have been interpreted as pertaining only to drug use that resulted in criminal consequences.

**RELEVANCE:** We must be sure applicants understand that an insurer generally has a right to know all the applicant knows regarding the state of his health and medical history. *Material* misrepresentations vitiate the policy. In fact, courts generally will allow an insurer to rescind the contract if an applicant misrepresents or omits even *one* material fact.

Materiality is determined solely by the probable and reasonable effect which *truthful* answers would have had upon the insurer. If an insurer requires answers to specific questions in the application, *that alone* is usually enough to establish materiality. So the question—the only relevant question—is whether the applicant misrepresented or omitted a fact would have affected the insurer’s decision to underwrite the contract. If the insurer would not have issued the policy if it had known the true facts, or if it would have charged a higher premium for the policy, materiality is established.

Note: An insurer does not have to prove actual intent to deceive. Both parties to a life insurance contract must deal fairly with each other. The insured has a duty to *read the contract and the application* in accordance with his or her representations and to report to the company any misrepresentations or omissions.

Nor is it a defense that, as in this case, the insured’s actual cause of death was unrelated to the misrepresentation. Rescission will be allowed whether or not there is any relation between the misrepresentation and the ultimate loss.

One last point: This case makes it clear that applicants generally have a duty to disclose to the insurer any material changes in his or her health that occur *after* he or she signs the application and *before* the policy is issued.

WRNewswire #7.29.14 was written by Steve Leimberg of [Leimberg Information Services, Inc. \(LISI\)](#) and [Leimberg & LeClair, Inc.](#)

#### **DISCLAIMER**

**In order to comply with requirements imposed by the IRS which may apply to the Washington Report as distributed or as re-circulated by our members, please be advised of the following:**

**THE ABOVE ADVICE WAS NOT INTENDED OR WRITTEN TO BE USED, AND IT CANNOT BE USED, BY YOU FOR THE PURPOSES OF AVOIDING ANY PENALTY THAT MAY BE IMPOSED BY THE INTERNAL REVENUE SERVICE.**

**In the event that this Washington Report is also considered to be a “marketed opinion” within the meaning of the IRS guidance, then, as required by the IRS, please be further advised of the following:**

**THE ABOVE ADVICE WAS NOT WRITTEN TO SUPPORT THE PROMOTIONS OR MARKETING OF THE TRANSACTIONS OR MATTERS ADDRESSED BY THE**

**WRITTEN ADVICE, AND, BASED ON THE PARTICULAR CIRCUMSTANCES, YOU SHOULD SEEK ADVICE FROM AN INDEPENDENT TAX ADVISOR.**

---

The AALU *WRNewswire* and *WRMarketplace* are published by the Association for Advanced Life Underwriting® as part of the Essential Wisdom Series, the trusted source of actionable technical and marketplace knowledge for AALU members—the nation’s most advanced life insurance professionals.